Riding ESG waves across the globe: the US and India in focus

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At any surf spot in the world, you can find a cadre of wetsuit-clad wave watchers scanning the horizon of the sea. Surfing, a sport unlike any other, demands an intricate understanding of the water and weather conditions. The interplay between tides and the underwater terrain determines the height, direction and formation of wave patterns.

At Comgest, we see the parallels between surfing and our own quality growth investment approach. Just as experienced surfers may wait hours before paddling out into the water and selecting a wave, we typically conduct years of fundamental research to determine whether a company meets our quality growth criteria. We seek companies that have exceptional longevity, visible growth, robust free cash flow, formidable barriers to entry, strong corporate culture and ESG credentials.

Environmental, social and governance (ESG) factors are integrated into our research, investment selection and portfolio management process. Like tidal patterns and swell size for surfers, ESG helps us discern what separates these quality companies from the rest. From our perspective, ESG provides us with an enhanced understanding of a company's quality and long-term growth potential.

NO TWO WAVES ARE THE SAME

In recent years, a global patchwork of ESG regulation has taken shape as policymakers attempt to address issues including climate change, human rights or biodiversity. From industry-wide pledges to net zero targets, there has been a tidal wave of new ESG commitments, regulations and rules since the launch of the Paris Agreement in 2015, which aims to prevent global temperatures from rising above 1.5°C and has been signed by nearly every country.

Emerging and developed economies face different challenges in balancing economic development with the pursuit of a more sustainable future. These market-by-market differences are akin surfing: no two waves are the same, but all surfers should consider the same fundamental elements - wind direction, tide break, water depth and swell size. When confronting markets with different "wave" patterns, we seek companies that possess deep competitive moats, solid ESG foundations and high visibility that have the potential to grow well into the future.

RIDING THE ESG PIPELINE IN THE US

Renowned for stunning waves and elite surfers, Hawaii's Banzai Pipeline is equally notorious for its extremely complex break points. Similarly, the ESG wave in the US, shaped by a variety of federal and state-specific rules and regulations, presents a formidable challenge for investors.

We believe that the US offers an attractive mix of qualities that make its companies appealing to investors, including its efficiency and corporate culture. Given its highly competitive market environment, we consider that strong US performers typically possess quality business models leveraging on their cutting-edge innovation, scale or unique brand image. Based on our experience, the sustainability strategy of companies can either reinforce or weaken their quality.

Copart, the leading US salvage car auction marketplace, exemplifies how a company's ESG approach can result in consistent long-term growth. The company collects and stocks vehicles deemed "non-repairable" by insurance companies and auctions them online. Copart customers then typically repair and reuse the cars with about 30% of auctioned cars hitting the road again.

From our perspective, Copart benefits from several competitive advantages that are key to its long-term growth, including its network size and relationship with insurance companies. Copart's marketplace is the largest in the world with over 200,000 cars and buyers in over 190 countries. The company operates over 200 locations across 11 countries, which means that it can efficiently pick up vehicles and add them to its wide range of stockyards.

PADDLING TOWARD GREATER TRANSPARENCY IN INDIA

Across the globe, India's ESG landscape is comparable to surf spots along Goa's coast, still early in development but growing in popularity. Unlike the Banzai Pipeline's towering waves, Goa is known for having more manageable beginner waves. However, with patience, quality waves can still be found.

India's embrace of ESG is similarly still in its early stages compared to more mature markets, such as the European Union. The country has taken steps to improve its ESG regulations, including implementing the Business Responsibility and Sustainability Reporting, a framework which requires the top 1,000 listed companies to disclose their ESG performance. In our view, this signals a growing emphasis on ESG transparency and improving quality of disclosure.

Power Grid Corporation of India, India's largest power transmission company is contributing to the country's rising energy demand and transition to renewables. More than 80% of its work-in-hand projects are focused on renewable energy transmission, helping to address the country's grid limitations. There are already signs that India's energy access has strained the country's unstable grid network. Between 2000 and 2022, India's electricity consumption increased by 223% with factors like urbanisation and construction fuelling growing power demand. We believe that Power Grid's transmission lines are crucial to meeting this increased energy demand and connecting India's renewable energy resources to the grid.

QUALITY IS THE KEY TO STAYING ON YOUR BOARD

Global markets have been battered by waves of uncertainty in recent years, including natural disasters, rising geopolitical rivalries and trade tensions. As long-term bottom-up stock pickers, however, we tend to look past short-term macro developments and keep our sights on company-specific drivers of growth. We seek companies with competitive advantages and strong ESG credentials, which will believe will position for sustainable earnings growth over time. In our view, these "all-weather" performers can face swells of macro headwinds and economic uncertainty – and emerge on the other side.

AUTHORS BIOS

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